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QUESTION PRESENTED FOR REVIEW

Whether section 318 of the Federal Power Act, 16 U.S.C. § 825q, prohibits the Federal Energy Regulatory Commission from limiting a utility to recovery of a "comparable market" price for coal purchased from an affiliated company when the Securities and Exchange Commission subjects the transaction to an "at cost" standard pursuant to the Public Utilities Holding Company Act, 15 U.S.C. §§ 79 *et seq.*

STATEMENT AS TO AFFILIATED COMPANIES

A list identifying the parent company and non-wholly owned subsidiary and affiliated companies of Ohio Power Company was provided at page i of the brief in opposition to the petition for certiorari.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1989

No. 89-1283

ARCADIA, OHIO, *et al.*,
Petitioners,

v.

OHIO POWER COMPANY, *et al.*,
Respondents.

On Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit

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BRIEF OF RESPONDENT OHIO POWER COMPANY

STATEMENT

Ohio Power Company (Ohio Power), as an affiliate of a registered utiiity holding company, is subject to regulation both by the Securities and Exchange Commission (SEC) under the Public Utility Holding Company Act of 1935 (PUHCA), 15 U.S.C. §§ 79 *et seq.*, and by the Federal Energy Regulatory Commission (FERC) under the Federal Power Act (FPA), 16 U.S.C. §§ 824 *et seq.* In 1972, Ohio Power began the development, through an affiliate, Southern Ohio Coal Company (Southern Ohio), of certain coal mines in order to assure a reliable supply

of coal for particular generating facilities.[1] As required by section 9 of the PUHCA, 15 U.S.C. § 79i, Ohio Power applied for and received the approval of the SEC for its investment in Southern Ohio. In accordance with section 13(b) of the PUHCA, 15 U.S.C. § 79m(b), and the applicable SEC regulations, the contract between Ohio Power and Southern Ohio specified that the sale be made "at cost."

This case results from the refusal of the FERC to permit Ohio Power to recover in its wholesale rates the amounts it is obliged to pay to Southern Ohio under the cost-based contract, limiting recovery instead to a hypothetical market price. On review, a panel of the United States Court of Appeals for the District of Columbia Circuit vacated the decision of the FERC.

1. The Statutory and Regulatory Scheme. The Public Utility Act of 1935, 49 Stat. 803, 15 U.S.C. §§ 79 *et seq.*, (the 1935 Act), was an integrated response to concerns arising from the dominance of public utility holding companies in the early part of this century.[2] Title I added the PUHCA, 15 U.S.C. §§ 79 *et seq.*, conferring upon the SEC broad authority to regulate public utility holding companies. Title II added Parts II and III of the FPA, 16 U.S.C. §§ 824 *et seq.*, conferring upon the predecessor to the FERC, the Federal Power Commission (FPC), the authority to review the reasonableness of rates charged by public utilities to their wholesale customers in interstate commerce.

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[1] We use "affiliates" in this brief in its commonly understood sense of related entities under common control, rather than in the technical sense in which the term is used in the PUHCA. 15 U.S.C. § 79b(a)(11).

[2] Federal Trade Commission, Utility Corporations, S. Doc. No. 92, Parts 72-A & 73-A, 70th Cong., 1st Sess. (1935) ("FTC Report"). The reports that formed the basis of the 1935 Act have been called "some of the most exhaustive and comprehensive studies ever to underlie a federal statute." *North American Co. v. SEC*, 327 U.S. 686, 701 n.11 (1946).

One of the abuses of principal concern was the sale of goods and services by holding company subsidiaries to affiliated utility operating companies at inflated prices, which were then reflected in artificially high rates to consumers. FTC Report, Part 72-A, pp. 64, 467, Part 73-A, pp. 63, 70. *See also* Report of National Power Policy Committee on Public-Utility Holding Companies, S. Rep. No. 621, 74th Cong., 1st Sess. 56 (1935). In response, Congress decided to limit holding companies to such other businesses "as are reasonably incidental, or economically necessary or appropriate to" their utility operations. 15 U.S.C. § 79k(b)(1). Further, to guard against unnecessarily high rates to consumers, affiliate transactions were barred except under such "terms and conditions" as the SEC "by rules and regulations or order shall prescribe . . . to insure that such contracts are performed economically and efficiently for the benefit of such associate companies at cost." 15 U.S.C. § 79m(b). The SEC is authorized to grant exemptions from the "at cost" requirement, by rule or order, if it determines that an exemption is "necessary or appropriate in the public interest or for the protection of investors or consumers" and if the transaction involves a foreign affiliate or "involve[s] special or unusual circumstances or [is] not in the ordinary course of business." *Id.*

The SEC has promulgated rules implementing section 13(b). Rule 90, 17 C.F.R. § 250.90 (1989), provides that, subject to certain exemptions, no transactions between holding company affiliates shall take place "at more than cost as determined pursuant to § 250.91 or any other applicable rule, regulation, or order of the Commission, or in the absence thereof, in accordance with sound methods of determining cost." In Rule 91, 17 C.F.R. § 250.91 (1989), the SEC specified the manner in which cost should be determined. In Rule 90(d)(2), 17 C.F.R. § 250.90(d)(2) (1989), and Rule 92, 17 C.F.R. § 250.92 (1989), the SEC provided an exemption and an

alternative standard for goods produced by the seller, stating that such goods shall not be sold "at a price which exceeds the price at which the purchaser might reasonably be expected to obtain comparable goods elsewhere."

Congress recognized that the regulatory responsibilities it assigned in the 1935 Act to the SEC and to the FPC could overlap. To ensure that regulated entities were not subject to duplicative regulatory requirements, Congress provided in section 318 of the FPA that when a person is subject to "a requirement of the Public Utility Holding Company Act of 1935 or of a rule, regulation, or order thereunder, . . . such person shall not be subject to the requirement of [the FPA], or of any rule, regulation, or order thereunder with respect to the same subject matter." 16 U.S.C. § 825q.

The FERC's regulations give effect to this provision in the case of fuel purchased from an affiliate:

> Where the utility purchases fuel from a company-owned or controlled source, the price of which is subject to the jurisdiction of a regulatory body, such cost shall be deemed to be reasonable and includable in the adjustment clause.

18 C.F.R. § 35.14(a)(7) (1989).[3]

2. The SEC's Review of Ohio Power's Coal Costs. Ohio Power is a wholly-owned subsidiary of the American Electric Power Company, Inc. (AEP), a registered public utility holding company that provides electric service at wholesale and retail over a seven-state area through

[3] "Adjustment clause" refers to a fuel adjustment clause, which is a mechanism through which increases or decreases in the cost of fuel (and, in some cases, other specified items) incurred by a utility are flowed through to ratepayers without the need for a rate filing. *See* 18 C.F.R. § 35.14(a)(1) (1989). Under cost of service regulation, a utility recovers its remaining costs of providing service through "base rates," which may be changed only through a rate filing with the appropriate regulatory agency.

eight operating companies. AEP is the nation's largest single user of coal. (R. 1664.) In the early 1970's, AEP anticipated that lower-sulfur coal, which would enable its generating plants to comply with new federal air emission standards, would become increasingly difficult and more costly to obtain. (R. 1534-35.) The urgency of these concerns was underscored by AEP's experience in the late 1960's, when coal prices rose dramatically and suppliers failed to honor commitments under long-term contracts, diverting coal to higher-priced spot markets. (R. 1535.) In addition, AEP then had under construction or in the planning stage 15,500 megawatts of generating capacity, which would require an additional 32.5 million tons of coal annually. (R. 1537.)

In 1971, the SEC authorized Ohio Power to create and to capitalize Southern Ohio, an affiliate, which would develop and operate coal mines "[i]n order to assure a reliable supply of coal for [Ohio Power's new] generating facilities." *Ohio Power Co.*, Holding Company Act Release No. 17383 at 1 (Dec. 2, 1971). The SEC specifically provided by order that "[t]he charges for coal by Southern Ohio will be based on an amount *equal to the actual cost* of Southern Ohio in developing the reserve and mining such coal," thereby indicating that the general standard set out in section 13(b) and Rules 90 and 91 would apply, and specified the manner in which the cost of capital was to be calculated. *Id.* at 2 (emphasis added). None of the coal to be mined by Southern Ohio was to be sold "to anyone other than public utility companies in the AEP system." *Id.* In accordance with this order, on October 1, 1972, Ohio Power entered into a contract with Southern Ohio, under which Ohio Power agreed to "receive, accept and pay for all of the coal produced by [Southern Ohio]," and to pay a price "equal to the entire cost to [Southern Ohio] of mining, preparing and delivering such coal." (R. 2676-77.) Subsequently, in a series of additional orders, the SEC reiterated that "[t]he price at which SOhio coal

is sold to AEP system companies *will not exceed* the cost thereof to the seller," the calculation of which was specified in some detail, approved Ohio Power's sale of coal mines and leases to Southern Ohio, approved borrowings by Southern Ohio to reduce its cost of capital, approved further investments by Ohio Power in Southern Ohio to finance efficiency improvements in mining operations, and required both Ohio Power and Southern Ohio to file quarterly financial information and statements setting out "the quantities of coal sold to each buyer, the price of such coal and the method used to compute the cost of coal sold."[4]

3. The FERC Proceedings. In 1982, Ohio Power made a rate filing with the FERC pursuant to section 205 of the Federal Power Act, 16 U.S.C. § 824d. All issues were settled except the extent to which Ohio Power could include its costs for "captive coal" purchased from Southern Ohio in its fuel adjustment clause.

As the Administrative Law Judge (ALJ) found, "[b]y 1978 the Martinka mine [operated by Southern Ohio] was in commercial operation and it was decided to use the Martinka coal at Mitchell [an Ohio Power generating unit that had previously experienced operational problems due to poor quality coal] and the results have been very favorable." (Jt. App., p. 15.) The higher quality coal enabled the generating unit to increase its effective availability from 62 to 74 percent, which produced savings to customers of 24 to 36 million dollars. (R. 1609-11.) The ALJ referred to the evidence showing "that it makes economic sense for OPCO to use a coal of the quality of that from the Martinka mine even if it is more expensive than the coal used in the past" as "persuasive" and "unchallenged." (Jt. App., pp. 47, 49).

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[4] *Ohio Power Co.*, Holding Company Act Release No. 20515, 14 SEC Docket 928, 929, 930 (1978) (emphasis added). *See also Southern Ohio Coal Co.*, Holding Company Act Release No. 21008, 17 SEC Docket 310 (1979); *Southern Ohio Coal Co.*, Holding Company Act Release No. 21537, 19 SEC Docket 1309 (1980).

Further, the Judge found that Ohio Power was prudent in acquiring rights to Martinka coal, that the Martinka mine has been "efficiently developed and operated" (*id.*, p. 69) and that the inclusion of such coal costs in Ohio Power's wholesale rates for the three years in question (1980 to 1982) was reasonable (*id.*, p. 75).

The FERC reversed. Without questioning the findings that Ohio Power was prudent to acquire the Martinka mine and that the mine had been efficiently operated, without even mentioning the benefits of assuring a long-term supply of high quality coal or the resulting savings realized by consumers, and dismissing as "fortuitous" the environmental benefits provided by the lower-sulfur coal (Pet. App., p. 47a), the FERC directed Ohio Power to refund the difference between the cost-based price paid to Southern Ohio and a calculated hypothetical market price (*id.*, p. 64a). The FERC viewed the application of a market standard to have been resolved in its earlier decision in *Public Service Co. of New Mexico*, 17 FERC Rep. (CCH) ¶ 61,123 (1981), *aff'd*, 832 F.2d 1201 (10th Cir. 1987), which did not involve a utility subject to section 13(b) of the PUHCA. It refused, either under section 318 of the FPA or its own rules, to defer to the cost-based method of pricing the Martinka coal mandated by the SEC's regulations and orders. With respect to the statute, the FERC concluded that "setting the intra-corporate price and setting rates are not the same subject matter which would bring section 318 into play." (Pet. App., p. 37a.) Although the FERC was uncertain as to the meaning of the SEC's orders, it concluded that, "[t]hey do not appear to mandate the cost-based price where a market price would be lower." (*Id.*, p. 36a.) The FERC ordered Ohio Power to revise its fuel adjustment clause to provide for the automatic recovery of "the comparable market price [for coal mined by Southern Ohio], regardless of whether the price is higher or lower than costs." (*Id.*, p. 63a.)

4. The Decision Below. The court below unanimously vacated the decision of the FERC. *Ohio Power Co. v. FERC*, 880 F.2d 1400 (D.C. Cir. 1989) (Pet. App., pp. 1a-28a). After noting that the FERC itself did not claim that its interpretation of section 318 was entitled to deference under this Court's decision in *Chevron, U.S.A., Inc., v. Natural Resources Defense Council, Inc.*, 467 U.S. 837 (1984), and its progeny, the panel majority found that such deference would not, in any event, be appropriate since section 318 was not entrusted to the FERC's administration. Recognizing that the FERC had, in effect, set a different price term than had been set by the SEC for the cost of affiliate coal, the court found "[t]he conclusion that the same subject matter is implicated is inescapable." (Pet. App., pp. 9a-10a.) Under the FERC's reasoning, the court observed, "there could never be a conflict between the SEC and FERC with respect to a matter not specifically enumerated in section 318" and it was not inclined to render "the residuary language of section 318 meaningless." (Pet. App., p. 10a.) Further, the court noted that regulation under the PUHCA included the charge that the SEC "exercise its power in the interest of consumers, as well as of investors and the public, and 'to insure that such contracts are performed *economically and efficiently*,' as well as 'at cost.' 15 U.S.C. § 79m(b) (emphasis added)." (Pet. App., p. 10a.)

As to the argument that there was no present conflict between the agencies' requirements as long as the market price was below cost, the court concluded that it is sufficient, under section 318, that a person is subject to a requirement under the PUHCA and that "[t]he fact that FERC's market approach produces a current result that does 'not exceed' cost" does not make the requirements of PUHCA inapplicable. (Pet. App., p. 14a.) Cognizant of this Court's precedents "that disfavor conflicting regulations resulting in trapped costs," *see, e.g., Nantahala Power & Light Co. v. Thornburg*, 476 U.S. 953 (1986), the majority found that the market-based test adopted by the FERC would impermissibly create trapped costs when applied to transactions regulated by the SEC under an "at cost" standard. (Pet. App., p. 16a.) In any event, the court concluded payment of a market-based price when it is in excess of cost cannot be reconciled with the SEC's cost limitation. (Pet. App., p. 18a.)

The third member of the panel agreed that the same subject matter, within the meaning of section 318, was before both agencies. (Pet. App., pp. 19a, 20a.) He concluded, however, that section 318 was inapplicable because there was no actual conflict between the requirements imposed by the two agencies as long as the market price to which the FERC limited Ohio Power was below the cost-based price mandated by the SEC. He noted that he, too, would find such a conflict, and would require that the FERC yield in favor of the SEC, if the market price imposed by the FERC were higher than the cost-based price. (Pet. App., p. 23a.) Although he disagreed on the issue of statutory construction, he agreed that the FERC's decision must be vacated for failure to comply with the FERC's own regulation (quoted, *supra* p. 4). The majority had no occasion to reach that issue.

SUMMARY OF ARGUMENT

The central underpinning of the FERC's order was its view that section 318 is inapplicable because "setting the intra-corporate price and setting rates are not the same subject matter which would bring section 318 into play." (Pet. App., p. 37a). A unanimous court below disagreed, holding that precisely the same subject matter—the reasonableness of the price that Ohio Power pays to Southern Ohio—was at issue. (*Id.*, pp. 9a, 20a.) Before this Court, both Petitioners and the Government abandon the FERC's "different subject matters" rationale. There is also agreement that Ohio Power is subject to a require-

ment imposed by the SEC with respect to that subject matter—that the transfer price be based on "cost." The FERC's attempt to substitute a different standard—market—for fixing that transfer price must fail because the SEC has spoken to the precise subject matter that the FERC seeks to regulate.

Before this Court, the FERC for the first time argues that its market price standard should be sustained if it is a "consistent, concurrent" requirement, and therefore does not conflict with the SEC's cost standard. The FERC requests a remand to allow the court below to determine whether, under the requirement imposed by the SEC, the transfer price must always be "at cost" or "not in excess of cost," thereby implying that the FERC's specification of a market price would be "consistent" with the cost requirement imposed by the SEC, if the SEC establishes only a ceiling price *and* if market is below cost.

There is no occasion for a remand. The FERC's order provides that the market standard applies *both* when the market price is below the cost-based price *and* when the market price is above the cost-based price. Indeed, the across-the-board application of the market test was central to the FERC's rationale, is required by the agency's precedents, and will, under the FERC's order, occur without further action by the agency. All members of the court below agreed that when the market price, as the FERC calculates it, is above the cost-based price—as has in fact sometimes been the case since the FERC's order was issued—there is a conflict between the regulatory requirements imposed by the FERC and those imposed by the SEC. It is of no import, therefore, whether the SEC has established an "at cost" price or only a cost limitation. In neither event is it possible to reconcile a market price in *excess* of cost. Even if section 318 applies only in cases of "actual conflict," the FERC's order must be reversed.

Instead of defending the FERC's actual order, Petitioners and the Government urge the Court to review

a hypothetical ruling, which the FERC expressly disclaimed any intention of making: the imposition of a lower-of-cost-or-market standard for affiliate transactions within holding companies. No purpose would be served by such review. Moreover, a lower-of-cost-or-market standard, which is tantamount to a prohibition on vertical integration by holding companies into non-utility businesses, is incompatible with Congress' objective in the PUHCA of permitting affiliate transactions that are "reasonably incidental, or economically necessary or appropriate to" the holding company's utility operations, 15 U.S.C. § 79k(b)(1), subject to a cost standard. Application of a lower-of-cost-or-market standard would stand "as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress," *Pacific Gas & Elec. Co. v. State Energy Resources Conservation & Dev. Comm'n*, 461 U.S. 190, 204 (1983), quoting *Hines v. Davidowitz*, 312 U.S. 52, 67 (1941), and would therefore conflict with the "at cost" standard specified in the PUHCA. As applied here, it would ensure that the AEP system will suffer significant losses on investments made to secure a reliable supply of operationally and environmentally preferable coal, even though the SEC approved the investment, and the FERC agreed both that it was a prudent commitment and that the mine has since been efficiently operated.

Finally, affirmance would not give rise to a regulatory gap of *any* proportion. Under the analysis of the court below, when the PUHCA or the SEC's rules and orders thereunder have not imposed a requirement with respect to a particular subject matter, the FERC is free to do so, assuming it otherwise enjoys legislative competence. The bond of regulatory protection is complete. In the final analysis, Petitioners' complaint appears not to be addressed to a regulatory gap, but to dissatisfaction with the allocation of regulatory responsibilty. That, however, is an issue for Congress.

ARGUMENT

I. SINCE NEITHER PETITIONERS NOR THE FERC DEFENDS THE INTERPRETATION THAT THE FERC GAVE TO SECTION 318, NO ISSUE REGARDING THE APPLICATION OF *CHEVRON* IS RAISED.

In its order in this case, the FERC held that it was free to apply a market test to Ohio Power's purchase of coal from Southern Ohio, because, in its view, different subject matters, within the meaning of section 318, were before the FERC and the SEC. (Pet. App., pp. 37a-40a.) Petitioners urged this Court to review this case principally because they believed the Court of Appeals paid insufficient deference, under *Chevron, U.S.A., Inc.*, and its progeny, to this interpretation of the statute. (Pet., pp. 12-13.) In their briefs on the merits, however, neither Petitioners nor the FERC (now joined by the SEC) even attempts to support the interpretation on which the agency's order was based. The FERC in fact contends that whether the FERC and the SEC have imposed requirements with respect to the same subject matter is irrelevant to the application of section 318. (FERC Br., p. 35 n. 23.) [5] There is thus complete agreement, as there was among the members of the court below (*see* Pet. App., p. 19a), that the same "subject matter" was before the FERC and the SEC. No issue of the degree of deference, if any, to be accorded the FERC's decision to the contrary is before the Court.

Petitioners and the FERC instead argue that an "actual conflict" between the requirements imposed by the SEC and those imposed by the FERC is necessary for section 318 to apply (the second question presented

[5] In the same vein, Petitioners now concede that in the case of conflict, "Section 318 deprives the FERC of its ratemaking authority" (Pet. Br., p. 17), disavowing the FERC's view that no decision of the SEC could affect its authority because the SEC does not set rates.

in the Petition). While we address the merits of this argument *infra*, it is important to recognize that it, too, raises no issue of deference because it does not support the FERC's order and was not relied upon by the agency.

The FERC's order discussed the regulations and orders of the SEC and concluded, "[t]hey do not appear to mandate the cost-based price where a market price would be lower, rather they permit a price up to a cost-based price," implying that section 318 did not apply in that situation. (Pet. App., p. 36a.) The FERC left no doubt, however, that it was not relying on the fact that, at the time of its order, market was lower than cost, because it was prescribing a market price "*regardless* of whether the price is higher or lower than costs." (*Id.*, p. 63a; emphasis added.)

The application of a market price test when market exceeds cost was central to the FERC's decision: "Under the rationale of tying affiliate coal costs to the comparable market price, not only must cost recovery be limited to the market price when actual costs exceed market price, but fuel charges *must* be allowed up to the market price, even if actual costs are less." (*Id.*; emphasis added.) The FERC characterized its decision as simply an application of the market-price test it announced in *Public Service Co. of New Mexico*, where it permitted a utility not subject to section 13(b) to recover the market price of coal purchased from an affiliate, which price exceeded cost. (Pet. App., pp. 42a-44a.) [6] Further, the FERC ordered Ohio Power to modify its fuel adjustment clause to provide for the recovery of an amount up to the market price for all coal purchased from Southern Ohio, without regard to whether market price exceeds cost. (Pet. App., p. 66a.) Because the fuel adjustment clause

[6] As the FERC noted (Pet. App., p. 42a), until the *New Mexico* decision, the FERC and the FPC applied a cost test to affiliate transactions.

operates automatically (*see supra* n. 3), no further action by the FERC is required for Ohio Power to recover the "comparable market" price when that price exceeds cost. In fact, the market price, calculated in accordance with the FERC's methodology, has exceeded the cost of mining Martinka coal in some months, and did so even before the FERC's order on rehearing was issued.[7]

It is common ground that an "actual conflict" exists when the market price exceeds the cost-based price, even if, as the FERC believed, the SEC's orders only establish cost as a ceiling.[8] Since the application of a market price in that circumstance was central to the FERC's rationale, the agency justified its disallowance of the coal costs incurred by Ohio Power by relying on its "different subject matters" reasoning, and did not even mention the fact (which it had noted earlier) that its market approach at that time produced a result that did not exceed cost. (Pet. App., pp. 61a-63a.) Therefore, even if the "no actual conflict" argument advanced by Petitioners in their petition and on brief had merit, it would not support the agency's orders. *See FPC v. Texaco, Inc.*, 417 U.S. 380, 397 (1974) (agency's order must be affirmed on the basis relied upon in its opinion, or not at all); *Burlington Truck Lines, Inc. v. United States*, 371 U.S. 156, 168 (1962) (rejecting "*post hoc* rationalizations" of appellate counsel). Although Petitioners and the FERC argue that deference should be paid to the FERC counsel's present position that an actual conflict is an additional prerequisite to the applicability of section 318, no justification has been offered for deference to an argument advanced by counsel, that, although mentioned in the agency's order, is inconsistent with the agency's rationale, does not support the agency action under review, and was not relied upon by the agency for that purpose. *See Bowen v. Georgetown Univ. Hosp.*, 109 S. Ct. 468, 473 (1988); *Investment Co. Inst. v. Camp*, 401 U.S. 617, 628 (1971).[9]

Since neither Petitioners nor the Government supports the FERC's interpretation that different subject matters were before the two agencies, no issue is presented regarding the deference, if any, to be given to that interpretation. Indeed, as Petitioners recognize (Pet., p. 12), the FERC's decision to prescribe a market test whether the market price is above or below cost could *only* be supported, if at all, on the "different subject matters" rationale. Once it is conceded that the same subject matter was before the FERC and the SEC, the FERC's decision *must* be vacated. No point would be served by undertaking a review of whether a different, hypothetical

[7] Market price exceeded cost in both November and December 1987. Ohio Power Co., Compliance Filing, FERC Docket Nos. ER82-533-004, *et al.* (May 9, 1988).

[8] The concurring member of the panel below noted, "if the market price determined by FERC were higher than cost . . . then FERC's requirement would clearly conflict with the SEC's requirement and, under section 318, FERC would have to abide by the SEC's determination." (Pet. App., p. 23a.) The FERC's request for a remand to determine whether the SEC's orders fix cost as the price, or only set a ceiling price (FERC Br., p. 11), indicates that the FERC, too, believes a conflict exists if market price exceeds cost. Petitioners have advised the Court that "the SEC's regulations merely establish an upper limit on the price SOCCO may charge" (Br., p. 15); that "the SEC regulations specifically prohibit the performance of sales contracts 'at more than cost.' 17 C.F.R. § 250.90(a)(2) (1989)" (*id.*, pp. 41-42); and that "the SEC orders relied upon by Ohio Power establish only a *ceiling* price on the coal" (*id.*, p. 43). Similarly, the Indiana Municipal Power Agency concedes that there would be a conflict if FERC authorized Ohio Power to pay in excess of cost. (Br., p. 17 n. 13.)

[9] Nor does the fact that the SEC has joined in the FERC's brief before this Court advance Petitioners' deference claims, especially since the brief does not support, and the SEC has thus not joined in, the FERC's "different subject matters" argument. *See ETSI Pipeline Project v. Missouri*, 484 U.S. 495, 516-17 (1988) (plain language of statute precludes Secretary of the Interior from exercising authority delegated to the Secretary of the Army, regardless of the latter's concurrence).

FERC ruling, limiting recovery in affiliate transactions to the lower-of-cost-or-market, would be consistent with the scheme of cost-based regulation under the PUHCA.[10]

II. THE COURT OF APPEALS CORRECTLY HELD THAT SECTION 318 PROHIBITS THE FERC'S PRESCRIPTION OF A MARKET TEST FOR A TRANSACTION SUBJECT TO THE COST STANDARD SPECIFIED IN SECTION 13(b) OF THE PUHCA AND IN THE IMPLEMENTING SEC REGULATIONS AND ORDERS.

Petitioners, joined by the FERC, contend that the principal failure of the Court of Appeals was its application of a "field preemption" analysis to determine the applicability of section 318. This contention and the related assertion that the analysis of that court could have far-reaching and untoward results mischaracterize the decision below. The repeated incantation of "field preemption" cannot obscure the failure of Petitioners and the Government to address whether "the same subject matter" was before the FERC and the SEC, or even to describe the bounds of the "field" from which they believe the decision below excluded the FERC. The Court of Appeals did *not* hold—as it would have had it employed a field preemption analysis—that the FERC, when operating in its own sphere of setting wholesale rates for electricity, was precluded by section 318 from regulating any aspect of transactions between affiliates within holding companies. *See Schneidewind v. ANR Pipeline Co.*, 485 U.S. 293, 298-99 (1988); *Rice v. Santa Fe Elevator Corp.*, 331 U.S. 218, 230 (1947). Instead, it determined that the FERC could not impose a "requirement" with respect to the narrow "subject matter" covered by section 13(b) of the PUHCA and the implementing rules and

[10] For this reason, the Court should consider dismissing the petition as improvidently granted. *See Jones v. Hildebrant*, 432 U.S. 183 (1977) (issue framed in the petition and passed upon below not advanced in oral argument).

orders of the SEC: the standard by which the reasonableness of the price in a transaction between holding company affiliates is determined. Only in this narrow "field" did the majority below find that the FERC was precluded from imposing additional requirements. This carefully channeled analysis, which flows directly from the plain language of section 318, hardly leads to the parade of horribles presented by Petitioners and the FERC.

Further, the court below went on to undertake precisely the "pragmatic analysis" now advocated by the FERC: it explored the purposes for which the SEC was directed by Congress to enforce a cost standard and probed the practical effect of the coexistence of the FERC's market price requirement and the requirement that had been imposed by the SEC. The court concluded that the FERC's market-price test, applicable whether market is above or below cost, is fundamentally incompatible with cost-based regulation of the Ohio Power-Southern Ohio transactions by the SEC. As we show below, the Court of Appeals' conclusion with respect to FERC's actual ruling was plainly correct. Further, even if the FERC had intended to impose a lower-of-cost-or-market test—which it clearly did not—such a ruling would stand as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress in enacting the PUHCA.

A. Section 318 Prohibits the FERC From Imposing a Market Test Because Ohio Power Is Subject to a Requirement Imposed By the SEC Under the PUHCA With Respect to the Price Standard To Be Applied to Its Purchase of Coal From Southern Ohio.

Section 318 of the FPA provides, in terms that are unmistakable, that if a person is "subject" to a requirement of PUHCA, "or of a rule, regulation, or order thereunder . . . such person shall not be subject to [a] requirement of [the FPA] or of any rule, regulation or

order thereunder, with respect to the same subject matter" absent the issuance of an exemption by the SEC. 16 U.S.C. § 825q. The court below found unanimously, and no one disputes before this Court, that the SEC and the FERC were each seeking to regulate the same subject matter—the price to be paid by Ohio Power for coal purchased from Southern Ohio. Nor, as we demonstrate presently, is that finding subject to credible challenge. The remaining question, under section 318, is whether Ohio Power is subject to a "requirement" imposed by the SEC with respect to that subject matter. Again, the issue is not subject to serious dispute. (Pet. App., p. 5a.)

In approving the purchase of coal from Southern Ohio, the SEC required that the price to be paid by Ohio Power be based on "cost." [11] Whether cost was to establish the price floor as well as the price ceiling is of no current moment. What is significant is that the PUHCA and the SEC's implementing rules and orders established the regulatory *standard* that is to govern the transfer price—cost. It is that very transfer price that the FERC seeks to regulate—the amount that it will credit

[11] In the absence of the SEC's orders, it might be open to question whether the market test laid out in the SEC's Rule 92 for goods produced by the seller applied instead. As the court below found, however, the SEC's orders leave no doubt that this transaction is governed by a cost standard: "Rules 90 and 91 are regulations under section 13(b) and as binding thereunder as an individualized order." (Pet. App., p. 15a.) This is consistent with the SEC's regulation of other fuel supply affiliations of registered holding companies, which were also regulated on a cost basis. *See, e.g., New England Elec. Sys.*, Holding Company Act Release No. 20632, 15 SEC Docket 329 (1978); *Central and South West Corp.*, Holding Company Act Release No. 22635, 26 SEC Docket 159 (1982). In the only case in which the SEC authorized a market-price test, it issued an express exemption from section 13(b), thereby giving the FERC discretion to regulate the rate consequences of the transaction. *New England Elec. Sys.*, Holding Company Act Release No. 22309, 24 SEC Docket 298, 305-08 (1981).

to Ohio Power as the price of coal purchased from Southern Ohio. This is precisely what the FERC may not do, because the SEC has by order imposed a requirement with respect to the precise subject matter that the FERC seeks to regulate.

As the court below found (Pet. App., pp. 9a-10a), the FERC's assertion that the "subject matter" of its rulings is "setting rates" (*id.*, p. 37a), which was not before the SEC, effectively reads the phrase "or any other subject matter" out of section 318. It is an interpretation of section 318 that is "manifestly contrary to the statute." *Sullivan v. Zebley*, 110 S. Ct. 885, 890 (1990); *Chevron, U.S.A., Inc.*, 467 U.S. at 844.[12] The SEC *never* directly sets wholesale rates for electricity, as the Congress that gave that authority to the FPC in 1935 well knew. Under the FERC's interpretation, then, section 318 would apply, if at all, only to the enumerated subjects. The FERC's restrictive interpretation contradicts the ordinary meaning of the inclusive residuary language. Further, it fails to give effect to all of the words of the statute and, accordingly, cannot be credited. *See, e.g., Crandon v. United States*, 110 S. Ct. 997, 1008 (1990) (Scalia, J., concurring); *Reiter v. Sonotone Corp.*, 442 U.S. 330, 339 (1979); *Sunshine Anthracite Coal Co. v. Adkins*, 310 U.S. 381, 392 (1940).

The structure and legislative history of the 1935 Act confirm the clearly expressed intent of Congress that the SEC, and not the FERC, regulate transactions between

[12] On brief, the FERC abandons this interpretation, asserting that it is irrelevant "whether the 'subject matter' as to which the SEC has imposed 'requirements' is the same as the 'subject matter' as to which FERC has imposed 'requirements.'" (FERC Br., p. 35 n. 23.) Statutory interpretation, however, must begin with the language of the statute. *Consumer Prod. Safety Comm'n v. GTE Sylvania, Inc.*, 447 U.S. 102, 108 (1980).

affiliates within utility holding companies by applying a cost standard.[13] We are in agreement with the Government that a principal aim of the Congress in enacting the 1935 Act was to curb the practice of passing inflated prices on to utility consumers as a result of inter-affiliate transactions. (FERC Br., p. 5.)[14] In response, Congress did not decide to bar holding companies from entering non-utility businesses, but instead to permit them to engage only in such other businesses "as are

[13] This Court has held that, "[i]n ascertaining the plain meaning of the statute, the court must look to the particular statutory language at issue, as well as the language and design of the statute as a whole." *K Mart Corp. v. Cartier, Inc.*, 486 U.S. 281, 291 (1988), citing *Bethesda Hosp. Ass'n v. Bowen*, 485 U.S. 399, 405 (1988). *See also Dole v. United Steelworkers*, 110 S. Ct. 929, 937 (1990) (statutory language unambiguous "in light of the language and structure of the Act as a whole").

[14] *See* 15 U.S.C. § 79a(b)(2). The FTC Report stated that its recommendation that affiliate transactions within holding companies be regulated was directed to an evil "which directly affect[s] the rate-paying public." FTC Report, Part 73-A, p. 70. Thomas Corcoran, one of the principal draftsmen of Title I of the 1935 Act, explained that while affiliate transactions at inflated prices also injured equity investors in operating utility subsidiaries of holding companies, such transactions were "unfair to the ratepayers, because ultimately the profit [to the holding company] has to come out of somebody." *The Public Utility Holding Company Act of 1935: Hearings on S.1725 Before the Senate Committee on Interstate Commerce*, 74th Cong., 1st Sess. 173 (1935) ("Senate Hearings"). FPC Commissioner Seavy agreed that both parts of the 1935 Act, the PUHCA and the FPA, were principally for "the benefit of the consumer," and explained that the PUHCA "affects the rates insofar as any unusual or unnecessary imposition of expenses upon the operating companies" is concerned. *The Public Utility Holding Company Act of 1935: Hearings on H.R. 5423 Before the House Committee on Interstate and Foreign Commerce*, 74th Cong., 1st Sess. 447-48 (1935) ("House Hearings"). *See also id.* at 343-45 (statement of Mr. Rayburn). Similar observations are found in the Congressional debate. 79 Cong. Rec. (1935) at 8391 (remarks of Sen. Norris); *id.* at 8392 (remarks of Sen. Shipstead); *id.* at 8399 (remarks of Sen. Costigan); *id.* at 8688-89 (remarks of Sen. Bone); *id.* at 8709-10 (remarks of Sen. Brown).

reasonably incidental, or economically necessary or appropriate to" their utility operations. 15 U.S.C. § 79k(b)(1). Congress also specified in section 13(b) that such transactions were to take place "at cost," to promote their economical and efficient performance and to protect consumers against paying excessive utility rates. 15 U.S.C. § 79m(b). Congress assigned the responsibility for regulating affiliate transactions within holding companies to the SEC, even though, in another part of the 1935 Act, it gave the FPC plenary authority over wholesale rates charged by utilities in interstate commerce. 16 U.S.C. §§ 824d, 824e.[15]

The specification of a cost standard in section 13(b) was both singular and deliberate. Alone among the substantive provisions of the 1935 Act, section 13(b) explicitly provides that affiliate transactions are to take place "at cost," rather than simply under a broadly defined public interest standard to be fleshed out by the agency.[16] This singularity is not accidental. The House

[15] As originally introduced, both the House and the Senate bills made regulation of affiliate transactions within holding companies the responsibility of the FPC, *not* the SEC. *See* H.R. 5423, 74th Cong., 1st Sess. §§ 12(a)-12(d) (1935); S. 1725, 74th Cong., 1st Sess. § 13(g) (1935). This feature was retained in the bill passed by the Senate, S. 2796, 74th Cong., 1st Sess. (1935). The House substitute bill, and ultimately the bill approved by the conference committee, placed authority over affiliate transactions in the SEC. *See* H.R. Rep. No. 1318, 74th Cong., 1st Sess. 7 (1935).

[16] The other provisions of the 1935 Act gave the FPC or the SEC broadly defined authority to regulate in a manner "necessary in the public interest," 16 U.S.C. § 824, "necessary or appropriate in the public interest," 16 U.S.C. § 824a, "compatible with the public interest," 16 U.S.C. § 824c, or "necessary or appropriate in the public interest or for the protection of investors or consumers," 15 U.S.C. §§ 79b, 79e, 79f, 79g, 79j, 79k, 79*l*, 79m(a), 79n, 79o, 79q, 79t. The FPC was directed to ensure that rates for transmission and wholesale sales of electricity in interstate commerce are "just and reasonable," 16 U.S.C. §§ 824d, 824e, but the standard against which justness and reasonableness was to be measured

substitute bill amended the original Senate bill by eliminating the requirement that transactions between affiliated companies be made at cost, replacing it with a more general requirement, which merely made it unlawful for affiliates to contract in contravention of such rules and regulations "as the [SEC] deems necessary in the public interest or for the protection of investors or consumers." *See* H.R. Rep. No. 1318, 74th Cong., 1st Sess. 6, 19 (1935).

Deletion of the "at cost" standard evoked a sharp dissent. Congressman Eicher decried the deletion of "the very definite principle" that "intra-system service arrangements must be on a cost basis." *Id.* at 45, 53. The conference committee, in apparent response, restored the "at cost" standard. *See* H.R. Rep. 1903, 74th Cong., 1st Sess. 72 (1935). The legislation was enacted in this form. 15 U.S.C. § 79m(b).[17]

The FERC's reading of section 318 to permit it to override this clearly expressed Congressional determination eviscerates the 1935 Act's regulation of affiliate transactions. The FERC nowhere explains how the SEC can fulfill the congressional mandate to protect consumers against excessive rates due to abusive affiliate transactions by applying a cost standard if, when the FERC sets wholesale rates, it ignores the SEC's implementation

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was not specified. *See FPC v. Hope Natural Gas Co.*, 320 U.S. 591, 602 (1944).

[17] Petitioners' argument that Congress' express reinstitution of the cost standard in section 13(b) somehow supports the authority of the FERC to disregard that standard (Pet. Br., pp. 29-30) is untenable. The general standard in the House substitute bill was rejected not because it would have given the SEC ratemaking authority, but because Congress wanted to leave no doubt that a cost standard should be applied to affiliate transactions in holding companies. The general grant of authority to the FPC over wholesale rates cannot override the simultaneous specific grant of authority to the SEC to regulate affiliate transactions, using a cost standard. *See Morton v. Mancari*, 417 U.S. 535, 550-51 (1974).

of Congress' directive, subjecting those transactions instead to a market test. In fact, the FERC's construction makes the SEC's regulation under section 13(b) pointless. The "intra-corporate price" (Pet. App., p. 37a)—a term that appears nowhere in the 1935 Act—has no impact on consumers unless that price is reflected in electric rates paid by consumers. The FERC cannot suggest that Congress enacted section 13(b) in order to regulate meaningless bookkeeping entries among commonly-owned entities. Further, under the FERC's construction of section 318, a regulated entity could not ascertain the standard to be applied to a contemplated affiliate transaction unless it obtained prior rulings from *both* agencies. This, however, is precisely the type of duplicative regulation that section 318 was designed to preclude. The FERC's reading of section 318 simply cannot be squared with the language of that section or the integrated legislative scheme of the 1935 Act.

B. Even if an Actual Conflict Is Required for Section 318 To Apply, the FERC's Application of a Market Test, Whether Market Is Above or Below Cost, to a Transaction Governed by Section 13(b) of the PUHCA Conflicts With That Provision and the SEC's Regulations and Orders Implementing It.

Before this Court, the FERC argues for the first time that section 318 must be read to permit "concurrent, consistent regulation" by the FERC and the SEC (FERC Br., pp. 12, 13, 23), and urges a remand so that the Court of Appeals may interpret the SEC's orders to determine whether the FERC's market test is in fact "consistent" with the requirements imposed by the SEC.[18] The Court of Appeals, however, undertook precisely the type of "pragmatic" assessment urged by

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[18] Petitioners similarly assert that Congress intended to create "dual, complementary regulatory regimes." (Pet. Br., p. 25.)

the FERC, concluding that the requirement imposed by the FERC cannot be enforced "without running afoul of the SEC's bar" on the payment of an inter-affiliate price in excess of cost. (Pet. App., p. 18a.) Even if section 318 applies only in instances of "actual conflict," the FERC's comparable market test, applicable whether the market price is above or below the cost-based price, is manifestly inconsistent with the regime of cost-based regulation of affiliate transactions within holding companies enacted by Congress and implemented by the SEC.

1. The FERC's application of a market test to transactions subject to cost-based regulation under section 13(b) does not amount to "concurrent, consistent regulation." As the Court of Appeals recognized, the cost test and the market test are different means to the same end: the protection of consumers against excessive rates attributable to affiliate transactions. (Pet. App., p. 11a.)[19] The FERC believes that a market test better serves that end. Where a holding company subject to the PUHCA is concerned, however, Congress has chosen a cost standard. Neither the FERC nor this Court is free to disregard Congress' unambiguously expressed prefer-

[19] Petitioners concede that section 13(b) of the PUHCA "was designed to avoid 'excessive charges' incurred as a result of inter-affiliate contracts" (Br., p. 6), while the FERC's mandate under the FPA is similarly "to protect ratepayers from excessive charges" (*id.*, p. 8). Congress clearly intended the SEC to have ongoing oversight over affiliate transactions, giving the SEC the power to require companies performing contracts subject to section 13(b) to preserve accounts and other records, to provide them for the SEC's inspection and to keep accounts in the manner prescribed by the SEC. 15 U.S.C. §§ 79o(d), 79o(f), 79o(i). The SEC may also require holding companies to file reports that include information the SEC deems "necessary or appropriate to keep reasonably current the information filed under section [13]," 15 U.S.C. § 79n, a requirement that has been imposed on the Ohio Power-Southern Ohio transaction.

ence; the FERC's attempt to do so is hardly "complementary" to the SEC's implementation of the congressional directive.[20] Permitting the FERC to "take action which it thinks will best effectuate a federal policy . . . in the face of a congressional limitation on its jurisdiction would be to grant to the agency power to override Congress." *Louisiana Pub. Serv. Comm'n v. FCC*, 476 U.S. 355, 374-75 (1986). If the 1935 Act "falls short of providing safeguards desirable or necessary to protect the public interest, that is a problem for Congress, and not the [agency] or the courts, to address." *Board of Governors v. Dimension Fin. Corp.*, 474 U.S. 361, 374 (1986). *See also K Mart Corp. v. Cartier, Inc.*, 486 U.S. 281, 323 (1988) (Scalia, J., concurring and dissenting).

The SEC has also recognized, in a prepared statement submitted in 1982 to a congressional committee contemplating amendment or repeal of the PUHCA, that application of a cost test and a market test to the same transaction is neither "consistent" nor "complementary." The Chairman of the SEC stated that section 318 "provides for deference to the [SEC's] jurisdiction under the [PUHCA] when the [PUHCA] and the [FPA] contain overlapping provisions" and, therefore, the concurrent application of a market standard by the FERC and a cost standard by the SEC created a situation in which "that portion of the industry represented by the registered holding company systems is now subject to a different federal standard for determining affiliate transaction prices than that applied to the rest of the industry." *The Public Utility Holding Company Act of 1935: Hearings on H.R. 5220, H.R. 5465 and H.R. 6134 Before the Subcommittee on Energy Conservation and Power of the Committee on Energy and Commerce*, 97th Cong., 2d Sess. 582-83 (1982) (footnote omitted). The only authorita-

[20] That the FERC is free to use a market approach where it has been delegated unfettered regulatory discretion is unquestioned. *See Public Serv. Co. of New Mexico.*

tive statement of the SEC, which the Court of Appeals described as "[t]he clearest statement by anyone associated with the SEC" with respect to this issue (Pet. App., p. 13a), holds that, by virtue of section 318, the PUHCA's cost standard applies to affiliate transactions within holding companies to the exclusion of the FERC's market standard—a view diametrically opposed to that expressed in the FERC's order in this case.

2. As discussed *supra* pp. 13-14, the application of its market test when market exceeds cost is central to the FERC's order and its underlying rationale. Moreover, the FERC's order currently authorizes Ohio Power to collect through its wholesale fuel adjustment clause the excess of market over cost. The conflict between the FERC's market test and the SEC's cost standard is therefore clear, even if, as Petitioners contend, the SEC's regulations and orders only establish cost as a ceiling. The court below correctly noted that the FERC could not explain "how OPCO can recover in its rates . . . a fair market value in excess of cost without runing afoul of the SEC's bar" on payments above cost. (Pet. App., p. 18a.) On this point, the panel below was unanimous. (*Id.*, p. 23a.)

The FERC makes no attempt to offer the explanation that the Court of Appeals found lacking. Instead, it suggests that "[t]he court [below] did not decide whether the SEC orders required that SOCCO sell the coal to Ohio Power at cost, or instead merely set cost as a ceiling." (Br., p. 11). Accordingly, it urges a remand "to the court of appeals so that the necessary inquiry into the meaning of the four SEC orders can be undertaken" (*id.* at 36), recognizing that that issue, if pertinent, is addressed to the court, and not to the FERC. However, the issue as to which the FERC seeks a remand is of no moment. If section 13(b) and the SEC's regulations and orders require the payment only of actual cost—no more and no less—the conflict is plain. The conflict is equally

apparent if they merely establish cost as a ceiling. Since the effect of the FERC order is to sanction the precise circumstance that all members of the panel below recognize will give rise to an irreconcilable conflict, the remand the Government seeks would serve no purpose.

C. The FERC's Application of a Market Test to a Transaction Governed by Section 13(b) of the PUHCA Conflicts With the Requirements Imposed By the SEC When the Market Price Is Below Cost.

Petitioners contend that there is no conflict between the requirements imposed by the two agencies because "[i]t is not physically impossible for Ohio Power to comply with the orders of both the SEC and the FERC," as long as the market price determined by the FERC is below the cost-based price, as it was at the time of the FERC's order. (Pet. Br., p. 43.) Petitioners also argue that "Ohio Power can simply absorb the difference between the 'cost' and the recovery permitted by the FERC under a market-based price." (*Id.*, p. 44.)[21] Petitioners

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[21] Petitioners also contend that none of the SEC's orders "*requires* Ohio Power to buy any coal from [Southern Ohio]" (Pet. Br., p. 42; emphasis in original), although they do not develop this point. In fact, this contention is immaterial and inaccurate. First, section 13(b) of the PUHCA clearly *requires* application of a cost standard to any affiliate transaction that is permitted to take place, except where the SEC grants an exemption. As the court below found (Pet. App., p. 5a), it is "unquestioned" that the transaction between Ohio Power and Southern Ohio, having received SEC approval under section 9, is subject to a "requirement" under section 13(b) and the implementing SEC rules and orders. Second, the SEC approved Ohio Power's investment in coal mining properties through Southern Ohio because of the need "to assure a reliable supply of coal for [new Ohio Power] generating facilities." *Ohio Power Co.*, Holding Company Act Release No. 17383 at 1 (Dec. 2, 1971). To ensure that utility consumers benefitted from these investments, the SEC restricted sales of coal mined by Southern Ohio to AEP system utility operating companies. *Id.* at 2. The 1972 contract between Ohio Power and Southern Ohio, which was entered into as a result of this approval and which provides part of the

thus recognize that their argument effectively prescribes a "lower-of-cost-or-market" test, but pronounce themselves unconcerned by the "trapping" of costs that would result. The short answer to Petitioners' contention is that the FERC expressly disclaimed any intention to subject affiliate transactions to a lower-of-cost-or-market standard, recognizing that such a standard would be inequitable, inefficient, and potentially unconstitutional. (Pet. App., pp. 61a-64a.) Petitioners thus ask the Court to review a hypothetical ruling that was not before the court below.

Even if the FERC's order were limited to the situation when market is less than cost and had been intended to prescribe a lower-of-cost-or-market test, there is no support in the language, structure or history of the 1935 Act for the narrow reading that Petitioners give to section 318. The only authority cited for the proposition that current "physical impossibility" is a prerequisite for conflict is a preemption case, *Pacific Gas & Elec. Co.*, 461 U.S. at 204. However, this Court's preemption precedents, including *Pacific Gas & Electric*, recognize that a conflict between state and federal regulatory schemes also exists when state regulation "stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress," *id.*, quoting *Hines v. Davidowitz*, 312 U.S. at 67, or when state regulation "interferes with the methods by which the federal statute was designed to reach [its] goal." *International Paper Co. v. Ouellette*, 479 U.S. 481, 494 (1987). *See also California v. FERC*, 58 U.S.L.W. 4591, 4595 (U.S. May 21, 1990) (No. 89-333). Limiting Ohio Power to a market

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security for the Southern Ohio financing approved by the SEC in 1979, *Southern Ohio Coal Co.*, Holding Company Act Release No. 21008, 17 SEC Docket 310, 311 (1979), is even more explicit, obligating Ohio Power to "receive, accept and pay for all of the coal produced by [Southern Ohio]." (R. 2676.) In fact, the FERC agreed that Ohio Power's decision to purchase coal from the Martinka mine was prudent. (Jt. App., p. 69; Pet. App., p. 65a.)

price when market is below cost indeed stands as an obstacle to the accomplishment of the full purposes and objectives of Congress in the PUHCA, and therefore presents an "actual conflict" with the requirement imposed by section 13(b), if a conflict is necessary for section 318 to apply.

1. *First*, nothing in the language or legislative history of section 318 signifies an intention to limit its application to instances where it is currently "physically impossible" for a regulated entity to comply with the requirements of the FERC and the SEC. Section 318 speaks not in terms of "impossibility," but in terms of the applicability of "requirements" with respect to "the same subject matter," 16 U.S.C. § 825q, directing an inquiry into the requirements that the SEC currently has in place and those the FERC seeks to impose. In this case, the SEC *has* imposed requirements: its current regulations and orders at a minimum set cost as a ceiling, while the FERC's current order limits Ohio Power to the "comparable market" price. Petitioners' reliance (Br., p. 18) on the heading of section 318 to limit the clear language of the statute is misplaced: "[T]he heading of a section cannot limit the plain meaning of the text." *Brotherhood of R.R. Trainmen v. Baltimore & O. R.R.*, 331 U.S. 519, 529 (1947). In fact, the heading of section 318 lends no support to Petitioners' "physical impossibility" argument. The heading, which reads, "Conflict of *Jurisdiction*," not "Conflict of Requirements," confirms that section 318 applies whenever there is a clash between the spheres of "jurisdiction" of the SEC and the FERC because each agency has imposed a "requirement" with respect to "the same subject matter." [22]

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[22] To the extent the statement of a single senator quoted by the Government (FERC Br., p. 25) is at all probative, that statement recognizes that section 318 is directed to "conflicts of jurisdiction," in order to prevent "duplication and overlapping," not only to circum-

Second, if the reach of section 318 were as limited as Petitioners contend, the section would be unnecessary. The 1935 Act contains *another* provision, section 21 of the PUHCA, which provides that "nothing in this chapter shall affect . . . the jurisdiction of any other commission . . . of the United States . . . over any person, security or contract, insofar as such jurisdiction *does not conflict* with any provision of this chapter or any rule, regulation or order thereunder." 15 U.S.C. § 79u (emphasis added). A similar savings provision in the Securities Exchange Act of 1934, 15 U.S.C. § 78bb(a), has been held, with respect to state regulation, to protect state authority by restating the Supremacy Clause, *see Leroy v. Great West. United Corp.*, 443 U.S. 173, 183 n.13 (1979), *i.e.*, to prohibit state regulation in circumstances of physical impossibility *or* when that regulation stands as an obstacle to the execution of the objectives of Congress in the manner specified by Congress. Section 318, which was intended to assure the primacy, and therefore the efficacy, of regulation under the PUHCA, surely cannot be read more narrowly than section 21, as Petitioners urge. Indeed, Congress declined to use section 21 (which was included in the original bills) as a drafting model when, in conference, it expanded section 318 to cover "any other subject matter," and thereby "enlarged [the scope of the section] to include *any* conflict arising under this bill." H.R. Rep. No. 1903, 74th Cong., 1st Sess. 75 (1935) (emphasis added).

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stances of impossibility or inconsistent requirements. Further, Petitioners' focus on whether it is possible at any given moment for an entity to comply with the dictates of both agencies would render the applicability of section 318 subject to constant change, in the absence of action by either agency, as the relationship between cost and market changes. Nothing in the language of section 318 suggests that the regulatory reach of the SEC and the FERC should fluctuate on a monthly basis with respect to the same transaction, or should vary between different transactions subject to the same statutory and regulatory requirements.

Limiting section 318 to instances of "physical impossibility," as Petitioners urge, in order to permit substitution of a market test for the cost standard Congress simultaneously reinserted in section 13(b), would be inconsistent with Congress' expansive purpose in modifying section 318.

Third, the "lower-of-cost-or-market" standard for which Petitioners contend does not appear in the 1935 Act. Indeed, such a standard was proposed, but Congress declined to adopt it for affiliate transactions.[23] Congress undoubtedly recognized that vertical integration could provide benefits not otherwise available, but that subjecting affiliate transactions within holding companies to such onerous requirements would amount to a *per se* rule against such transactions.[24] Congress decided against

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[23] The FTC recommended that Congress prohibit affiliate transactions within holding companies "at more than cost or at more than the open market rates, whichever is less." FTC Report, Part 73-a, p. 71. (A similar standard was also contained in an alternative proposal advanced by Representative Pettengill. *See* House Hearings, pp. 700-01.) The bills originally introduced in the House and the Senate appear to have carried out this recommendation, banning all transactions between a utility and its holding company affiliates, except with a mutual service company organized so as to ensure:

> performance of service, sales and/or construction contracts . . . for member companies (1) at cost fairly and equitably allocated among such member companies, and (2) at a substantial saving to member companies over the cost . . . of comparable contracts if performed by independent persons.

H.R. 5423, 74th Cong., 1st Sess. § 12(g) (1935); S. 1725, 74th Cong., 1st Sess. § 13(g) (1935). *See also* Message of President Roosevelt, quoted in H.R. Rep. No. 1318, 74th Cong., 1st Sess. 2 (1935). This standard was enacted in section 13(d), 15 U.S.C. § 79m(d), applicable to mutual service companies, but was discarded in favor of the "at cost" standard enacted in section 13(b) for other affiliate transactions.

[24] The SEC Staff has stated that a standard based on "the lower of cost or market would be an effective means of prohibiting captive

banning affiliate transactions, instead subjecting them to cost-based regulation by the SEC. In this manner, utility customers would receive the benefits of vertical integration by holding companies into businesses determined to be "economically necessary or appropriate" to the holding company's utility operations. 15 U.S.C. § 79k(b)(1).

Application of a lower-of-cost-or-market standard would be particularly inappropriate in this case. As the nation's largest single user of coal, which it utilized to provide reliable electric service to millions of customers, AEP was understandably concerned about the price and supply upheaval that rocked the coal markets in the late 1960's and the implications of the Clean Air Act amendments of 1970 for the availability of lower-sulfur coal. (R. 1534-36, 1664). To assure both a reliable supply of coal and price stability, AEP undertook an extensive effort to secure a portion of its coal supplies, capable of meeting one-third of its annual requirements, from mines subject to its control. Ohio Power's investment in Southern Ohio was part of this program and, like each such investment, required and received the approval of the SEC.[25] In reliance on the "at cost" standard of section 13(b), which assured that customers receive the benefits

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mines. It would make such investments improvident on their face . . . [which] avoid[s] the need to consider the claimed advantages of captive mines." Comments of the Division of Corporate Regulation of the Securities and Exchange Commission on the Federal Energy Regulatory Commission Staff Preliminary Report of Investigation in FERC Docket No. E-9206, Dated July 31, 1978 at 18 n. 15 (Oct. 27, 1978) ("SEC Staff Comments").

[25] *See supra* pp. 5-6 and *Ohio Power Co.*, Holding Company Act Release No. 22770 (Dec. 10, 1982); *Blackhawk Coal Co.*, Holding Company Act Release No. 21672 (Aug. 7, 1980); *Appalachian Power Co.*, Holding Company Act Release No. 18363 (Apr. 3, 1974); *Appalachian Power Co.*, Holding Company Act Release No. 17507 (Mar. 23, 1972); *Ohio Power Co.*, Holding Company Act Release No. 16932 (Dec. 14, 1970).

of the affiliated operation, Ohio Power invested over $57 million in the Martinka mine, and a total of $299 million in Southern Ohio. The FERC affirmed the findings of its ALJ, based on unrebutted evidence, that Ohio Power "was prudent in acquiring rights to the Martinka coal . . . that the Martinka mine has been efficiently developed and operated" (Jt. App., p. 69), and that the use of Martinka coal significantly improved the performance of an Ohio Power generating unit, which "justifie[d] paying about $12-$18 per ton more for a more suitable coal" (*id.*, p. 48-49).[26] Now, years after the investment has been made and the beneficial results achieved, Petitioners argue that, because it is not "physically impossible" for Ohio Power to recover a "market" price that is below cost, Ohio Power should be denied recovery of the cost-based price upon which the investment was premised. Nothing in section 318 or the 1935 Act as a whole supports such a result.

2. None of the precedents interpreting section 318 supports Petitioners' strained view that the statute applies only when compliance with both regulatory schemes was "physically impossible" at the time the agencies' orders were issued.

The only previous time the interplay between the FPA and the PUHCA was before this Court was in *Northwestern Electric Co. v. FPC*, 321 U.S. 119 (1944), where a utility subsidiary of a holding company challenged the authority of the FPC to prescribe and apply to it a system of accounts, arguing, *inter alia*, that the regulation was "in conflict with the powers and the regulation of the Securities and Exchange Commission." *Id.* at 125. The Court rejected this contention, without citing section 318. The Court's discussion, in its entirety, was as follows: "[A]n examination of the statute and of the or-

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[26] The FERC's order stated that the ALJ's decision "is affirmed and adopted to the extent it is not inconsistent with this Opinion." (Pet. App., p. 65a.)

ders and proceedings of the Securities and Exchange Commission satisfies us that no conflict exists." *Id.* As the FERC notes (Br. at 15), a letter from the Chairman of the SEC was appended to the Government's brief in *Northwestern Electric.* The letter explained that some provisions of the PUHCA are not self-executing, and:

> Until the S.E.C. does by rule or order impose "requirements" pursuant to the sections which are not self-operative, there can be no conflict of requirements and Sec. 318 does not apply. It was not intended that utility companies should be able to thwart regulation by the F.P.C. by conjuring up . . . conflicts with *potential* action of the S.E.C.

Resp. Br. App. D at 98-99, *Northwestern Elec. Co. v. FPC*, 321 U.S. 119 (1944) (emphasis in original). Significantly, the letter did not include section 13(b) in the list of sections of the PUHCA that are not self-operative. *Id.* at 99.

By specifying that the possibility of "*potential* action" imposing a requirement was insufficient to implicate section 318, the SEC was acknowledging that the appropriate inquiry was whether the SEC has actually imposed requirements applicable to the subject matter at issue (or whether Congress has done so with respect to self-executing provisions). The SEC based its view that section 318 was inapplicable on the fact that its Rule U-27 (17 C.F.R. § 250.27 (1941)) adopted the FPC's accounting system for electric companies not already subject to it. *Id.* at 99-100. In its brief, the Government also noted that the SEC's Rule U-26 (17 C.F.R. § 250.26 (1941)) exempted utilities subject to the FPC's accounting system from the SEC's uniform system of accounts. *Id.* at 59 n.44. The SEC also considered it important to emphasize that the FPC's action at issue, requiring the utility to make a correction to its earned surplus account, was "fully consistent" with the purpose of the SEC's regulation under section 12(c) of the PUHCA: "to protect financial integrity and to prevent payment of dividends

out of capital or unearned surplus." *Id.* at 104. The SEC thus found section 318 inapplicable by determining that neither the PUHCA nor the SEC's rules had imposed a requirement with respect to the subject matter at issue, a conclusion buttressed by the fact that the requirement imposed by the FPC was compatible with "the accomplishment and execution of the full purposes and objectives of Congress." *Pacific Gas & Electric*, 461 U.S. at 204.

Appalachian Power Co. v. FPC, 328 F.2d 237 (4th Cir.), *cert. denied*, 379 U.S. 829 (1964), also involved an accounting issue. The court noted that, under Rules U-26 and U-27, the SEC "does not require utilities to keep their books in accordance with its requirements," and, indeed, "explicitly excepted" utilities from its uniform system of accounts under the PUHCA. *Id.* at 250. The court determined that the purpose of the SEC's accounting regulation under the PUHCA was to ensure that "the financial statements filed with it be prepared in a manner which provides adequate and fair disclosure." *Id.* at 250-51, quoting Accounting Series, Release No. 85 (Holding Company Act, Release No. 14173) (1960). The court found no "incompatibility" between this purpose and the FPC's requirement that its accounts—which had been adopted by the SEC—be used in the company's public financial reports. *Id.* at 252.[27]

The analysis undertaken by the Court of Appeals in this case was entirely consistent with those in *Northwestern Electric* and *Appalachian Power.* The court

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[27] The FERC (Br. at 27 n. 14) also relies upon *Mississippi Industries v. FERC*, 808 F.2d 1525, 1550, *reh'g granted and vacated in part on other grounds*, 822 F.2d 1104 (D.C. Cir.), *cert. denied*, 484 U.S. 985 (1987). This reliance is misplaced. As the court below correctly recognized (Pet. App., p. 13a), section 318 was inapplicable in *Mississippi Industries* by its terms because the contract at issue concerned the sale of electric energy, which is, by definition, excluded from any "requirement" under the PUHCA. 15 U.S.C. § 79b(a)(20).

reached a different result because it found it "unquestioned" that Ohio Power is subject to requirements promulgated under the PUHCA with respect to the purchase of coal from Southern Ohio (Pet. App., p. 5a) and it determined that the FERC's application of market test cannot be reconciled with the SEC's concurrent application of a cost standard. The court's conclusion that an actual conflict was not a prerequisite to the application of section 318 (Pet. App., p. 14a) does not suggest any lack of allegiance to *Northwestern Electric* and *Appalachian Power*. Since the only "actual conflict" argument presented to the court was based on "[t]he fact that the FERC's market approach produces a current result that does 'not exceed' cost," a fact the court correctly found immaterial (*id.*), the court was simply rejecting the "physical impossibility" requirement, which cannot be found in the earlier cases.

3. Petitioners acknowledge (Br., p. 44) that interpreting section 318 to apply only in the cases where it is "physically impossible" to comply with the requirements of the FERC and the SEC inevitably creates a situation in which a portion of the price that Ohio Power is required to pay to Southern Ohio, under the contract and the SEC's orders and regulations, is "trapped" by virtue of the FERC's denial of rate recovery. The Court of Appeals recognized that this Court's decisions in *Nantahala*, 476 U.S. at 970-71, and *Mississippi Power & Light Co. v. Mississippi ex rel. Moore*, 487 U.S. 354 (1988), "disfavor conflicting regulation resulting in trapped costs." (Pet. App., p. 16a-17a.) Though Petitioners and the FERC argue that these cases are inapposite because they involved instances in which Congress had "preempted the field" of regulation of wholesale electric rates, the analyses in these cases did not rest on that ground.

The Court did *not* hold in either *Mississippi Power & Light* or *Nantahala* that Congress' occupation of the field of wholesale electric rate regulation precluded the states

from exercising any authority over the manner in which costs incurred in wholesale transactions were reflected in retail rates. *See Nantahala*, 476 U.S. at 967-68.[28] Rather, the Court held that if a state's "undoubted jurisdiction over retail sales" were deemed to empower it to reexamine issues underlying wholesale rates fixed by the FERC, "impermissible interference . . . with the scheme of federal regulation" would result. *Id.* at 970. In both cases, the Court found that "[a] state must . . . give effect to Congress' desire to give FERC plenary authority over interstate wholesale rates, and to ensure that the States do not interfere with this authority." *Mississippi Power & Light*, 478 U.S. at 373, quoting *Nantahala*, 476 U.S. at 966.

The implications of this analysis for this case are clear. The FERC's "undoubted jurisdiction" over wholesale rates does not empower it to redetermine the appropriate pricing of the transaction between Ohio Power and Southern Ohio, requiring Ohio Power to "pretend that it is paying less for the [coal] it receives from [Southern Ohio], under agreements not subject to [the FERC's] jurisdiction, than is in fact the case." *Nantahala*, 476 U.S. at 971. Its attempt to subject this transaction to an inconsistent standard constitutes "impermissible interference . . . with the scheme of federal regulation" under the PUHCA (*id.* at 970), and fails to "give effect to Congress' desire to give [the SEC] plenary authority over . . . [transactions between holding company affiliates and] interfere[s] with this authority." *Mississippi Power & Light*, 487 U.S. at 373. The SEC's enforcement of the

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[28] Counsel for Petitioners here, representing the Appellant in *Mississippi Power & Light*, explained, "Under *Nantahala*, state ratemaking authority is preempted in only one limited respect. . . . [T]he state commission retains plenary authority to determine all other components of retail revenue requirements[,] . . . to design the specific rates under which the utility may recover its revenue requirements and to determine the manner and time frame in which extraordinary expenses will be recovered." Appellant's Reply Br., pp. 1-2.

congressional determination that consumers and the public interest are best protected by application of a cost standard to affiliate transactions within holding companies would be frustrated if the FERC were free to apply a different standard to these transactions. There is therefore an unmistakable conflict between the FERC's orders in this case and the requirements imposed by the SEC under section 13(b).

The fallacy in Petitioners' attempt to read a current "physical impossibility" requirement into section 318 is also apparent from the Court's recent decision in *California v. FERC*. There the Court held that a state's attempt to specify a higher minimum flow rate for a hydroelectric dam than was required by the license issued by the FERC was preempted. Even though it would not have been "physically impossible" for the licensee to comply with both minimum flow requirements (by simply meeting the higher state minimum requirement), the Court stated, "[a]llowing California to impose significantly higher minimum stream flow requirements would disturb and conflict with the balance embodied in" the FERC's licensing decision. 58 U.S.L.W. at 4595. The state provision thus stood "as an obstacle to the accomplishment of the full purposes and objectives of Congress." *Id.*, quoting, *Silkwood v. Kerr-McGee Corp.*, 464 U.S. 238, 248 (1984). The Court also noted that hydroelectric licensees had "considerable reliance interests" in the long-standing interpretation of the regulatory scheme. *Id.* at 4594.

Here, too, allowing the FERC to limit recovery to a market-based price because there is "room" below the cost-based price mandated by the SEC (viewed as a ceiling) would defeat the balance between the interests of consumers and investors that is reflected in section 13(b) and the implementing SEC regulations, amounting to precisely the type of "bleeding" of a utility subsidiary of

a holding company that Petitioners acknowledge (Br., p. 31 n.12) was of concern to Congress. *See* 15 U.S.C. § 79a(b)(1). Ohio Power's investment of over $299 million in Southern Ohio, approved by the SEC beginning almost twenty years ago, in order to provide reliable coal supplies for key generating units, surely represents a "considerable reliance interest" no less worthy of protection.

Even if Ohio Power were somehow able to retain the excess when market exceeds cost, the FERC's imposition of a market test would still fly in the face of Congress' decision that, through the cost standard, customers should receive those benefits. Section 11 of the PUHCA makes it apparent that Congress intended the decision as to whether a holding company will be permitted to enter a non-utility business to turn on whether the transaction was expected to produce benefits for the system's utility customers, *i.e.*, to be "economically necessary or appropriate" to the system's utility operations. 15 U.S.C. § 79k(b)(1). The FERC's market test would instead turn the decision into one based on the holding company's likelihood of realizing profits. An interpretation of section 318 that permits the FERC to undermine the basis of regulation under the PUHCA in this manner is plainly contrary to the statute.

D. The Decision Below Does Not Create a Regulatory Gap.

Petitioners and the Government argue that affirmance of the decision below necessarily would create a "regulatory gap" of significant proportion, in contravention of the comprehensive regulatory scheme intended by enactment of the Public Utility Act of 1935. Their parade of horrors (Pet. Br., pp. 32-34; FERC Br., pp. 26-27, 34-35) is misplaced. It proceeds from their mistaken assumption that the decision below is grounded on broad "field preemption" principles and from a misunderstanding of both the PUHCA and the FPA.

1. Nothing in the decision below restricts the authority of the FERC to regulate subject matters as to which neither the PUHCA nor the SEC's regulations and orders thereunder impose a requirement. The Court of Appeals' analysis was *not* premised upon the existence of "authority to regulate, even if unexercised" (Pet. Br., p. 24), but upon the requirements actually imposed by the statute and by the SEC's rules and orders.[29] Its conclusion that the FERC and the SEC were addressing the same subject matter and its finding that the FERC's order could not be reconciled with the "bar" explicit in the SEC's rules and orders led the court to find that the FERC had overstepped its bounds. The "early" agency decisions relied upon by the Government do not advance its cause. In *In re Evans*, 1 F.P.C. 511 (1937), the Federal Power Commission observed that "[a]s a result of the operation of section 318 of the Act [it] *is excluded* from jurisdiction over certain phases of the reorganization" (*id.* at 515; emphasis added), suggesting that the FPC considered itself ousted of even "concurrent, consistent" regulation over the aspects of the transaction regulated by the SEC. But as to those matters not subject to SEC-imposed requirements, the FPC exercised its regulatory discretion. *Id.* at 516-517. *In re Olcott Falls Co.*, 3 F.P.C. 310 (1942), is precisely to the same effect. The FPC recognized its ability to fill the gaps left unregulated by the SEC. What it declined to pass on, however, was the appropriateness of an acquisition of utility assets, which, if subject to the SEC's review under PUHCA, would be "exempt from the requirements of section 203 of the Federal Power Act by section 318 of that Act." Indeed, the FPC made clear that "in the first instance" the question of whether the acquisition was subject to a requirement under the

[29] As the letter of the SEC Chairman introduced in *Northwestern Electric* makes clear, a "requirement" may be imposed by the PUHCA itself, as well as by the SEC's rules or orders.

PUHCA relates to "the applicability of provisions of the Holding Company Act, and we therefore express no opinion on it pending a decision by the Securities and Exchange Commission which is charged with the administration of that Act." *Id.* at 312. Finally, the failure of the "regulatory gap" contention is manifest from the Government's discussion of *Appalachian Electric Power Co.*, 27 S.E.C. 1029 (1948), where the SEC indicated that the FPC was free to regulate the "consequences" of the approval that the SEC had given—that is, to regulate the terms of the sale of power from a generating company the formation of which the SEC had authorized—subject to the SEC retaining the prerogative of ensuring consistency with the requirements of PUHCA.

2. There is absolutely no basis for concern that utilities within holding company structures will be free to integrate vertically into non-utility areas without regulatory scrutiny. The PUHCA gives the SEC plenary authority over a holding company's expansion into a non-utility business, by virtue of section 9(a)(1). 15 U.S.C. § 79i(a)(1). An acquisition of an interest in any business is not to be approved if it "will tend towards interlocking relations or the concentration of control of public utility companies, of a kind or to an extent detrimental to the public interest or the interest of investors or consumers," 15 U.S.C. § 79j(b)(1), or if the business is not "reasonably incidental, or economically necessary or appropriate to the operations of such integrated public-utility system." 15 U.S.C. § 79k(b)(1).[30]

[30] The SEC has developed a "functional relationship" test to implement this standard. *See Michigan Consol. Gas Co. v. SEC*, 444 F.2d 913, 916 (D.C. Cir. 1971). One factor considered under this test is whether an affiliate transaction would provide a benefit not available through transactions with third parties. *See Public Serv. Co. of Oklahoma*, 45 S.E.C. 878, 884 (1975) (approving investment in oil and gas exploration venture as a means of meeting fuel requirements "when traditional purchases under long-term contracts are unavailable or are subject to curtailments or interruption").

It was pursuant to, and in total conformance with, this statutory structure that the Ohio Power-Southern Ohio relationship was forged. In fact, as noted *supra* p. 32 and n. 25, all of AEP's affiliated fuel supply operations were subject to SEC review and approval. Plainly, no "regulatory gap" exists.

3. Neither the FERC's ability to determine wholesale rates, nor its ability to pass on the disposition of utility assets, nor its ability to regulate accounting matters, is called into question by the decision below.

First, under *Appalachian Electric Power Co.*, although the SEC has authorized a transaction, the FERC remains free to regulate the consequences of the transaction for wholesale rates, provided that in so doing it does not do violence to requirements imposed by the SEC pursuant to the PUHCA. The FERC's proper role under the 1935 Act is to decide, in setting wholesale rates, *how* to apply determinations of the SEC, made pursuant to the PUHCA, but *not* to disregard those determinations.[31] In addition to assuring that a utility does not recover in rates an amount greater than cost, determined as specified by the SEC, and determining the manner in which that cost will be reflected in rates, the FERC may also integrate the pricing formula fixed by the SEC with the other considerations affecting the overall level of rates. *Cf. Nantahala*, 476 U.S. at 967-68. The FERC may even intervene before the SEC to urge the SEC to exercise its authority under section 13(b) to grant exemptions from the cost standard in an appropriate case. That the FERC may not, in addition, refuse to apply the "at cost"

[31] The division of the SEC Staff responsible for enforcement of the PUHCA has explained that "[t]he SEC pricing orders are final orders directed . . . to fixing a pricing formula," but the rate-making authority "has jurisdiction to try issues, both of fact and of interpretation, in *applying* such orders, insofar as material, to a particular rate case." SEC Staff Comments at 3 (emphasis added) (R. 7916).

standard mandated by section 13(b) of the PUHCA to a transaction unquestionably subject to that provision, does not demonstrate the existence of a regulatory gap.

Second, the decision below has no effect on the FERC's authority over utility divestitures. As the FPC recognized in *In re Olcott Falls*, section 318 is inapplicable in that situation because different "persons" are involved—the SEC has jurisdiction over the acquirer, the FERC over the entity disposing of utility assets (unless the SEC also has jurisdiction over that entity under section 12(d) of the PUHCA, 15 U.S.C. § 79*l*(d)).[32] In fact, in both *In re Olcott Falls* and *In re Evans*, the FPC passed on the appropriateness of a disposition under section 203 of the FPA, 16 U.S.C. § 824b.

Finally, the FERC's comprehensive authority to regulate the books of account of public utilities, 16 U.S.C. § 825(a), is not threatened by the decision below, which, like the decisions in *Northwestern Electric* and *Appalachian Power*, focused on the requirements, if any, imposed by the SEC. The FERC accounting authority, indeed, is assured by section 20(b) of PUHCA, 15 U.S.C. § 79t(b). In that section Congress, although giving the SEC a role in prescribing accounting standards for holding companies, prohibited accounting requirements by the SEC that are "inconsistent" with those "prescribed under the provisions of any law of the United States." The SEC has recognized the force of this prohibition and from the outset has directed companies subject to the

[32] *Amicus* American Public Power Ass'n argues (Br., p. 8) that, under the same analysis, section 13(b) applies only to the seller in an inter-affiliate transaction, not to the utility buyer, and so section 318 is inapplicable. The flaw in this argument (which does not appear in the FERC's orders) is that section 13(b) only applies when both the buyer and the seller are affiliates within the same holding company. The buyer is necessarily subject to the requirements of section 13(b), which *must* be the case if the manifest purpose of the provision—to protect utility subsidiaries of holding companies and their customers from exploitation—is to be served.

PUHCA to keep their books of account "in the manner currently prescribed for similar companies by the Federal Power Commission." 17 C.F.R. § 250.27(a) (1989). Indeed, that is precisely the rationale that underlies *Northwestern Electric* and *Appalachian Power*.

Thus, the bond of regulatory protection is complete. If the PUHCA or the SEC's rules or orders do not impose a requirement with respect to any subject matter and the FERC would otherwise be authorized to act, the FERC may do so. What the FERC may not do is what it attempted to do here: substitute its policy judgment for that of the SEC with respect to matters that Congress has delegated to the latter. In the final analysis, Petitioners' complaint appears to be addressed more to their dissatisfaction with the nature of SEC regulation—indeed, with section 13(b) itself. As to that, however, the court below correctly found (Pet. App., p. 11a) that their petition must be addressed to Congress. *See Board of Governors v. Dimension Fin. Corp.*, 474 U.S. 361, 373-74 (1986).

III. IF IT IS NECESSARY TO REACH THE OTHER FLAWS IN THE FERC'S DECISION, THE CASE SHOULD BE REMANDED TO THE COURT OF APPEALS.

The concurring member of the panel below found that, wholly apart from section 318, the FERC's decision violated the plain language of the agency's own regulation, 18 C.F.R. § 35.14(a)(7) (1989), which provides that, where the price of fuel purchased by a utility from an affiliate "is subject to the jurisdiction of a regulatory body, such cost shall be deemed to be reasonable and includable" in wholesale rates. (Pet. App., p. 28a.) Petitioners argue (Br. at 44-45) that the concurring judge erred in concluding that the phrase "shall be deemed" cannot be interpreted to create only a rebuttable presumption of reasonableness, rather than a conclusive

presumption. (Pet. App., pp. 24a-25a.)[33] They contend that several courts, including this Court, have construed the same phrase to create only a rebuttable presumption.

We are compelled to point out that Petitioners' reliance on *Lavine v. Milne*, 424 U.S. 577 (1976), for this proposition is based on an incomplete reading of the state law at issue in that case. Petitioners assert that the statute provided that a person who applies for welfare assistance within 75 days after voluntarily terminating his employment "shall be 'deemed' to have done so . . . for the purpose of qualifying for such assistance . . ." (Pet. Br., p. 45, quoting 18 N.Y. Soc. Serv. Law § 131 (11) (Supp. 1975); final ellipses in Pet. Br.) They fail to note, however, that this sentence goes on to provide that the applicant shall be deemed to have terminated his employment for the stated purpose "in the absence of evidence to the contrary supplied by such person." 18 N.Y. Soc. Serv. Law § 131(11) (Supp. 1975), quoted in *Lavine v. Milne*, 424 U.S. at 579. The Court's conclusion that this statute merely clarifies the assignment of the burden of proof to the applicant for assistance, 424 U.S. at 584, is unremarkable in light of the complete language of the statute. Since, however, the FERC's regulation at issue contains no counterpart to the "in the absence of evidence to the contrary" language in the New York statute, the decision in *Lavine v. Milne* has no bearing on this case.[34]

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[33] The concurring judge held that no deference was owed to the FERC's interpretation of the regulation because it was "at odds with the plain meaning of the text." (Pet. App., p. 24a.) He also held that "courts construing the word 'deemed' have generally found that it establishes a conclusive presumption." (*Id.*, citations omitted).

[34] The other federal decisions relied upon by Petitioners offer no more support for their claim. First, the statute at issue in *Hardy v. Lomenzo*, 349 F. Supp. 617, 621 (S.D.N.Y. 1972), like that in *Lavine v. Milne*, provided expressly for the introduction of evidence on the point ultimately at issue, a provision that cannot be found

The panel majority had no occasion to consider whether the FERC's decision violated the terms of its regulation because it found section 318 dispositive. (Pet. App., p. 19a.) No member of the court below reached Ohio Power's argument that the FERC's decision was arbitrary and capricious in that it compared the price Ohio Power paid for coal under its contract with Southern Ohio to a "comparable market" construct that was deficient in numerous respects. As an example, the FERC calculated its market comparison price by including coal with a substantially higher sulfur content than the Southern Ohio coal (up to 4% sulfur, when Southern Ohio coal averaged 1.5% sulfur), as well as coal of the type that had caused operating inefficiencies at the Ohio Power generating unit, which were remedied by the Southern Ohio coal. (Pet. App., p. 46a; Jt. App., pp. 47-48.) It is only through this manipulation of the "comparable market" that the FERC was able to find the cost-based price of Southern Ohio coal excessive.

Since these contentions were not considered below, if it is necessary to reach them this case should be remanded to the Court of Appeals for that purpose. *See Patrick v. Burget*, 486 U.S. 94, 99 n. 5 (1988); *J. Truett Payne Co. v. Chrysler Motors Corp.*, 451 U.S. 557, 568 (1981).

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in the FERC's regulation. *Gaither v. Myers*, 404 F.2d 216, 218 (D.C. Cir. 1968), did *not* hold that statutory language providing that any person operating a vehicle "with the consent of the owner, express or implied . . . shall . . . be deemed to be the agent of the owner" creates a rebuttable presumption. This language, the court stated, "provides a new substantive rule of law." *Id.* at 219. *Another* clause in the statute, providing that ownership of a vehicle involved in an accident "shall be *prima facie* evidence" that the driver has the consent of the owner, was held to establish a rebuttable presumption to that effect. *Id.* at 218. In *Bowers v. United States*, 226 F.2d 424, 428 (5th Cir. 1955), the majority found that the phrase "shall be deemed" was intended to operate not merely as a "presumption of fact rebuttable or otherwise, but as the [conclusive] statement of a substantive rule of law."

CONCLUSION

For the foregoing reasons, the decision of the United States Court of Appeals for the District of Columbia Circuit should be affirmed.

Respectfully submitted,

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